Regional Comprehensive Economic Partnership (RCEP) – what it means for international trade

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RCEP in brief

On 15 November 2020, fifteen Asia Pacific countries signed the "Regional Comprehensive Economic Partnership" (RCEP) agreement. The member countries include the 10 ASEAN member states of Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam, as well as Australia, China, Japan, New Zealand and South Korea.

RCEP is expected to enter into force either late 2021 or early 2022. Although it will be the world's largest free trade agreement (FTA) when measured by combined GDP (26 trillion dollars), population (2.27 billion) and total export value (5.2 trillion dollars) of signatory parties, it is not so clear whether it will be as large when it comes to market access and competitiveness of imported goods and services.

Although the Asia-Pacific region is already awash with FTAs, the establishment of RCEP will still have an important impact. Not only is it signed at a time when free trade is under pressure around the world, it links the three mammoths in Asia through an FTA (China, Japan and South Korea) and allows for enhanced regional supply chains for trade in goods.

Companies doing business in the region should perform an impact assessment early in order to take full advantage of RCEP's benefits when the agreement comes into effect. Given that most RCEP members already have existing FTAs with most other RCEP members, this is also a good time to review benefits that other FTAs already may offer to ensure an overall FTA strategy is optimised.

RCEP in more detail – trade in goods

The RCEP does not replace any of the existing FTAs that its members have between them, either on a multilateral or bilateral basis. Instead, it adds an additional dimension to regional economic collaboration. Although it is not quite as wide or deep as some of the existing agreements, its final text has still exceeded the expectations of many observers. The agreement includes 20 chapters in total, covering commitments in areas such as trade in goods, trade in services, investments, intellectual property, e-commerce, competition, government procurement and dispute settlement.

The trade in goods chapter will likely be the most important, or at least most immediately impactful, chapter of the RCEP for many companies. Key provisions under this chapter to take note of include:

- **Duty elimination**. Tariffs will eventually be eliminated for 90 percent of the trade in originating goods between member countries. Some tariff lines will have duties removed immediately when the RCEP enters into force, while others will see duties eliminated over a period of time. There are also product categories that may not be subject to duty reduction at all. Industries most affected will be those that traditionally carry high duty rates, such as food, agriculture, consumer good and automotive. It should also be noted that tariff reductions may vary depending on the precise RCEP country of origin. For example, a product originating in – say – New Zealand, may still be subject to a different reduced rate of duty to one originating in – say – China, when imported into South Korea.

- **Rules of origin**. All members have agreed to apply consistent rules of origin for all products. This means that once you can demonstrate a product meets the RCEP origin criteria, it will do so in all member countries. This is a critical benefit under RCEP as companies do not have to worry about satisfying multiple rules across different agreements.

- **Cumulation**. Originating materials from any RCEP member that are used in another member as inputs in the production of another product can be counted as originating content when determining the origin of the subsequent product. This will be an important benefit over other available FTAs as it offers greater flexibility on sourcing.

- **Certification of origin**. A notable provision that is not present in many other agreements in Asia is the gradual introduction of self-certification of origin. Initially, only authorized exporters will be allowed to self-certify the originating status of exported goods. All other exporters will be required to apply for certificates of origin from an issuing authority in the country of export. However, after an initial transition period, member states will be required to allow exporters and producers to self-certify origin by producing a so-called Declaration of Origin.

  For most RCEP members, the agreement does not initially allow for importers to self-certify originating status. The agreement provides that member states are to conduct a review following RCEP's entry into force regarding whether to allow self-certification by importers.

- **Duty refunds**. Importers who do not claim RCEP benefits at the time of importation may retroactively apply for duty refunds based on the duty rate under RCEP. In practice, this is likely limited to importers that indicate at the time of import that they are planning to use this facility in future.

- **Harmonisation of non-tariff barriers.** Customs procedures, inspections and quarantine measures, and technical standards will be gradually unified, which will contribute towards promoting the development of new cross-border supply chains and enhance the free flow of goods.

RCEP in more detail – other aspects

Although the other aspects of regional economic partnership are less clearly defined and will be harder for companies to benefit from in the short term, companies ignore them at their own peril. A few highlights include the following.

- **Trade in services**. A very wide phrase, covering many aspects of modern economic life. The agreement offers plenty of opportunities for many service providers to offer their trade in other RCEP members. As commitments are very member and industry specific, every company should evaluate the most appropriate mix of opportunities for itself. It should be noted that some members apply a “negative list” (meaning everything is covered unless it is mentioned on this list), while others apply a positive list (meaning only those services as listed will be open to operators from other RCEP members). Also note that although at a macro-economic level a negative list is often a sign of better opportunities than a positive list, at a micro-economic (company) level the reverse may be the case.

- **Protection**. The chapters on ***competition***, ***e-commerce***, ***intellectual property*** and ***investment*** are very much focused on protecting companies so that they have a fair chance to make the most of their business commitments to RCEP. Although not as deep, commitments tend to go beyond those at World Trade Organization (WTO) level and those already agreed to in existing FTAs.

- **Government procurement.** In a marked addition to the ASEAN+1 agreements, the RCEP makes specific provisions for government procurement. Although the practical impact may be muted to start with, focusing especially on transparency, it is a step in the right direction, especially given the increased levels of government stimulus around the region as a result of the COVID-19 pandemic.

- **Accession of new members**. To be well positioned for growth in the future, RCEP includes a provision to allow non-member countries to submit an expression of interest to join the agreement. This provision will take effect 18 months after the agreement enters into force.

PwC Observations

Before entering fully into force, the RCEP will require a ratification process to be completed by all member countries. The agreement will only take effect after at least six ASEAN member states and three non-ASEAN member states have completed ratification. This can sometimes be a relatively quick process but can also take years in some countries. We expect the agreement to enter into force for most members either in the second half of 2021 or in early 2022.

Compared to other modern regional agreements such as the CPTPP and the ASEAN Trade In Goods Agreement, RCEP has less coverage in terms of depth of many commitments and offers a slower reduction of tariffs. RCEP is also a relatively complex agreement with certain countries having different tariff reduction schedules for different countries of origin within RCEP. The mix of positive and negative lists for trade in services is another example of complexity. It will be important for companies to navigate these differences across the agreement when assessing impact.

Nevertheless, the RCEP will likely have an important impact on the Asia-Pacific region. It will enhance economic integration, promote free trade and facilitate economic growth. Through the formation of stronger value chains across the region, RCEP will also encourage companies to shift focus towards Asia and to intra-regional trade. Historically many Asian exporters have had their focus firmly on the big and rich consumer markets in North America and Europe, but that may well chance, especially as growth is more likely to come in Asian markets.

RCEP will also be the first FTA that Japan has with China and with Korea. This makes RCEP an important agreement for all three countries. For all members, there are many pre-existing FTAs which means there are several trade agreements currently available for companies that can be used today and may already give the benefits offered by RCEP. This should be taken into consideration when assessing the impact of RCEP to ensure the most beneficial agreement is being used.

What you can do to prepare

While RCEP is expected to only enter into force in a year or so, companies doing business in Asia Pacific should perform an impact assessment to determine the benefits available. When doing so, the benefits that other FTAs already offer should be reconsidered, as they may have changed since they were last looked at. Comparing benefits already available under existing FTAs to the benefits RCEP may add will allow companies to develop an optimal overall FTA strategy.

Once the RCEP enters into force, origin compliance management and proactive application of preferential tariff treatment should be prioritised to optimise RCEP benefits. Implementation details on additional tariff reductions, customs procedures, inspections, quarantine measures and other technical standards should be actively monitored to further reduce the costs and enhance efficiencies in the supply chain. Some aspects of implementation are left to the discretion of member states, and it may be in a company's interest to lobby for a particular type of implementation.

Impact on supply chain planning

The US-China trade war and the COVID-19 pandemic are recent and current challenges that have forced many companies in Asia-Pacific to start thinking about long term supply chain planning. Building a more resilient business model and being prepared to respond to disruption are key priorities for many companies today and will likely become more important going forward. The signing of RCEP can have an important role to play in this respect. The signing in itself will have an immediate impact by sending a positive message on how the leading economies in the Asia-Pacific are looking towards free trade and maintaining multilateral trading systems as the solution to promote economic growth and recovery. Not only will this help the region to build a stronger foundation to encourage greater regional collaboration, but also to shift focus towards Asia form elsewhere when important supply chain decisions are being made.

In addition, the RCEP may ease some of the pressure companies feel to diversify their manufacturing footprint. With better market access possible through existing facilities, more drastic changes to physical supply chains may be put on hold for a little while.

To discuss any of the above aspects of the RCEP in specific, or Asian FTAs in general, please contact the below mentioned.

Let's talk

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